KPMG

Understanding the SEC's climate rule

What you should know now

—

March 2024

visit.kpmg.us/ESGreporting

Understanding the SEC's climate rule

Background

— March 2021: The SEC requested public input on climate-related disclosures to help evaluate its then current rules and guidance.

— March 2022: The SEC proposed climate disclosure rules. Over the last two years, the SEC considered more than 4,500 unique comment letters as it drafted its final rules.

The final rule

— March 6, 2024: The SEC issued final rule, The Enhancement and Standardization of Climate-Related Disclosures for Investors.

— Changes from the proposal include simplified financial statement disclosures (see Q3), reduced requirements for the disclosure of GHG emissions (see Q4) and extended phase-in periods (see Q8).

— US companies currently preparing for compliance with ISSB™ Standards and/or ESRSs are well positioned as they begin to analyze the SEC's climate rules.

What you will find here

— Ten key aspects of the final rules.

— Practical considerations as you implement the requirements of the rules.

Abbreviations and key terms >

10 questions and answers to get you started

01 Who and what are in scope?

02 At a glance, what's required where?

03 What financial statement disclosures are required?

04 What GHG emissions disclosures are required?

05 What climate risk disclosures are required?

06 How do the different disclosures connect?

07 What are the implications for controls?

08 When must registrants comply?

09 How do the rules compare to other frameworks?

10 What do you need to do now?

1. Who and what are in scope?

Nearly all SEC registrants are in scope

- All domestic (US) registrants
- FPIs
- Companies filing registration statements, including IPOs

Registrant-based exclusions

- Canadian issuers reporting under the MJDS on Form 40-F
- Asset-backed issuers

Requirements-based exclusions

- Non-accelerated filers, and all entities that qualify as SRCs and EGCs, are not required to disclose GHG emissions; all other requirements apply

1) Disclosures are based on the same cadence and timing as the annual report, except for GHG emissions disclosure relief (see Q4).

2) Disclosures are less extensive than other sustainability reporting frameworks (see Q9), except for the financial statement disclosures (see Q3).

3) Discuss with your auditor how the rules will impact your annual financial statement or integrated audit.

2. At a glance, what's required where?

Disclosures are filed, not furnished

— In a note to the audited financial statements, disclose certain quantitative and qualitative information about (see Q3):

  – Severe weather events and other natural conditions
  – Material effects on financial estimates / assumptions
  – Carbon offsets or renewable energy credits / certificates

— In a separate 'climate-related disclosure' section of the annual report or registration statement, disclose certain quantitative and qualitative information about:

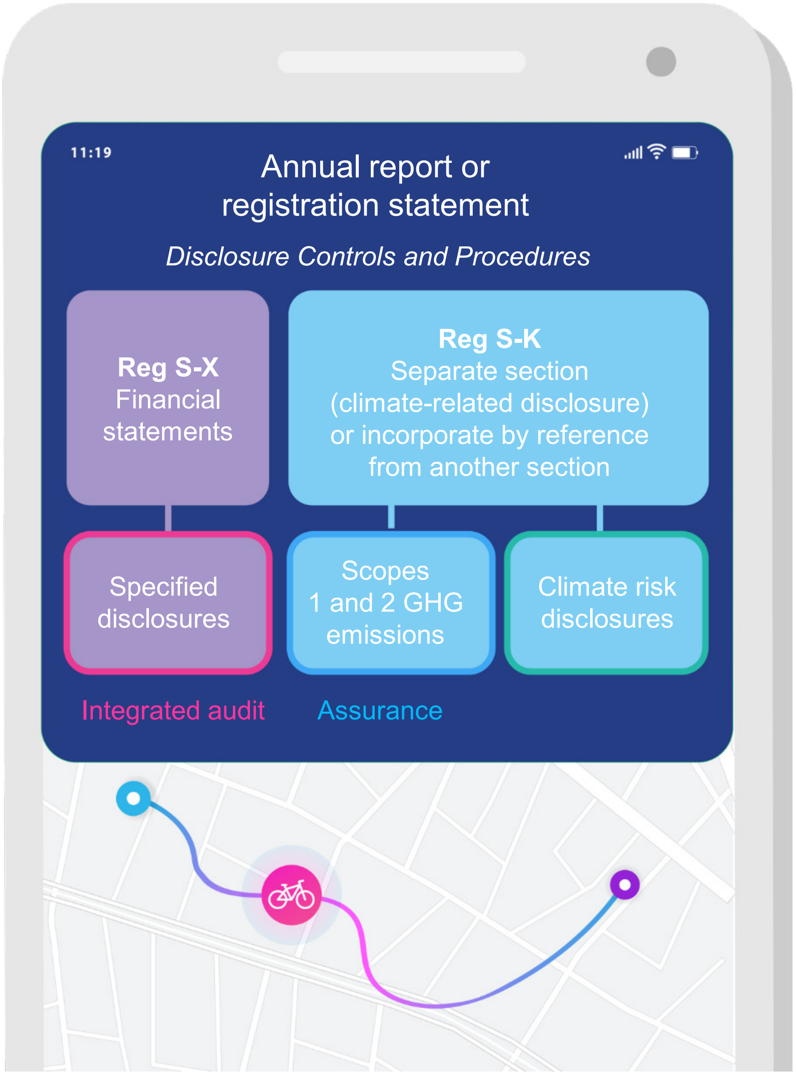
  – For larger registrants, Scopes 1 and/or 2 GHG emissions, if material (see Q4)
  – Climate risks (see Q5)

Robust control environment required (see Q7)

— All disclosures are subject to disclosure controls and procedures, and the financial statement note disclosures are subject to ICFR

— An ICFR audit of the financial statement notes is required for registrants subject to Section 404(b) of the Sarbanes-Oxley Act

— GHG emissions are subject to assurance for larger registrants



1) The definition of materiality is consistent with the materiality concept already used by the SEC.

2) An assessment of materiality is based on both quantitative and qualitative factors.

3) The rules include specific thresholds for the financial statement disclosures (see Q3) and materiality considerations for GHG emissions (see Q4).

4) Other disclosures focus on material impacts or what is reasonably likely to have a material impact over the short- and long-term.

3. What financial statement disclosures are required?

Attributable to severe weather events and other natural conditions

- Capitalized costs and charges (excluding recoveries)
  - If the aggregate amount of capitalized costs and charges is ≥ 1% of the absolute value of stockholders' equity or deficit at the end of the relevant fiscal year
  - No disclosure if aggregate for fiscal year < $500,000
- Expenses and losses (excluding recoveries)
  - If aggregate amount of expenditures expensed as incurred and losses is ≥ 1% of the absolute value of income or loss before income tax expense or benefit for the relevant fiscal year
  - No disclosure if aggregate for fiscal year < $100,000
- Material effects on financial estimates / assumptions

Attributable to any targets, goals, transition plans disclosed in the filing

- Carbon offsets and RECs that are a material part of the plan
- Material effects on financial estimates / assumptions

ILLUSTRATIVE DISCLOSURES

A. Related to severe weather events and other natural conditions:

	Balance sheet $	Income statement $
Capitalized costs and charges:		
Inventory	XX	
PP&E	XX	
Expenditures expensed as incurred and losses:		
General & administrative		XX
Other income / (loss)		XX

B. Related to targets / goals disclosed in the filing:

Carbon offsets / RECs at Jan 1	XX
Capitalized during the year	XX
Expensed	(XX)
Carbon offsets / RECs at Dec 31	XX

(A) and (B) accompanied by appropriate contextual information (e.g. accounting policies, significant inputs, assumptions, judgments made)

C. Material effects on financial estimates / assumptions:

As a result of our [disclosed] transition plan, we plan to accelerate the replacement of ABC assets. As a result, we have reduced the estimated useful lives of those assets from X to Y years.

1) Incorporate required disclosures into your financial reporting process.
2) Apply the 'attribution principle' to help simplify calculations – e.g. were increased incidences of flooding a 'significant contributing factor' in costs incurred to move storage facilities?
3) Design mechanisms to identify and tag transaction amounts that may need to be aggregated.
4) Design processes and identify relevant controls to monitor estimates and assumptions that may be materially impacted.

4. What GHG emissions disclosures are required?

Gross Scopes 1 and/or 2, if material

— Required for large accelerated filers and accelerated filers, except for SRCs and EGCs

— No specific approach prescribed

— Disclose methodology, significant inputs and significant assumptions used, including the organizational boundaries, operational boundaries and protocol or standard used – with details about calculation approach, data and tools

Disclosure relief

— Include statement in annual report indicating that GHG disclosures will be:

– Incorporated by reference from Form 10-Q for Q2 in the following fiscal year; or

– Included in an amended annual report on Form 10-K or 20-F no later than the due date for the Q2 Form 10-Q, or 225 days after the end of the fiscal year for FPIs

Assurance required

— Phased timeline starts with limited assurance for large accelerated and accelerated filers, moving to reasonable assurance for large accelerated filers only (see Q8)

— Additional disclosures apply when voluntary assurance is obtained

	Scope 1			Scope 2		
	20X6	20X5	20X4	20X6	20X5	20X4
CO_2						
CH_4						
N_2O						
NF_3						
HFC						
PFC						
SF_6						
Totals						

Disclose in CO_2e

Disclose if material

Disclose comparatives if previously disclosed in filings

Disclose gross – i.e. excluding offsets

Disclose disaggregated gases, if individually material

Materiality

The rules emphasize qualitative considerations in assessing materiality – e.g. is disclosure necessary to enable investors to understand whether you have made progress toward achieving a target or goal or a transition plan that you have disclosed under the final rules?

1) Write a GHG accounting manual, documenting details of methodologies, significant inputs, assumptions and boundaries used.

2) If you have a GHG inventory, assess your current processes and controls over the preparation and disclosure of your GHGs.

3) Review our Handbook, GHG emissions reporting, for guidance on how to apply the GHG Protocol and other tips, including interoperability considerations.

5. What climate risk disclosures are required?

Processes for identifying, assessing and managing material climate-related risks

Physical and transition risks that materially impact or are reasonably likely to have a material impact over the short- and long-term

Climate risk mitigation, adaptation: Whether and how climate-related risks are part of the business model, strategy, financial planning, capital allocation

Oversight by the board and management, including management expertise

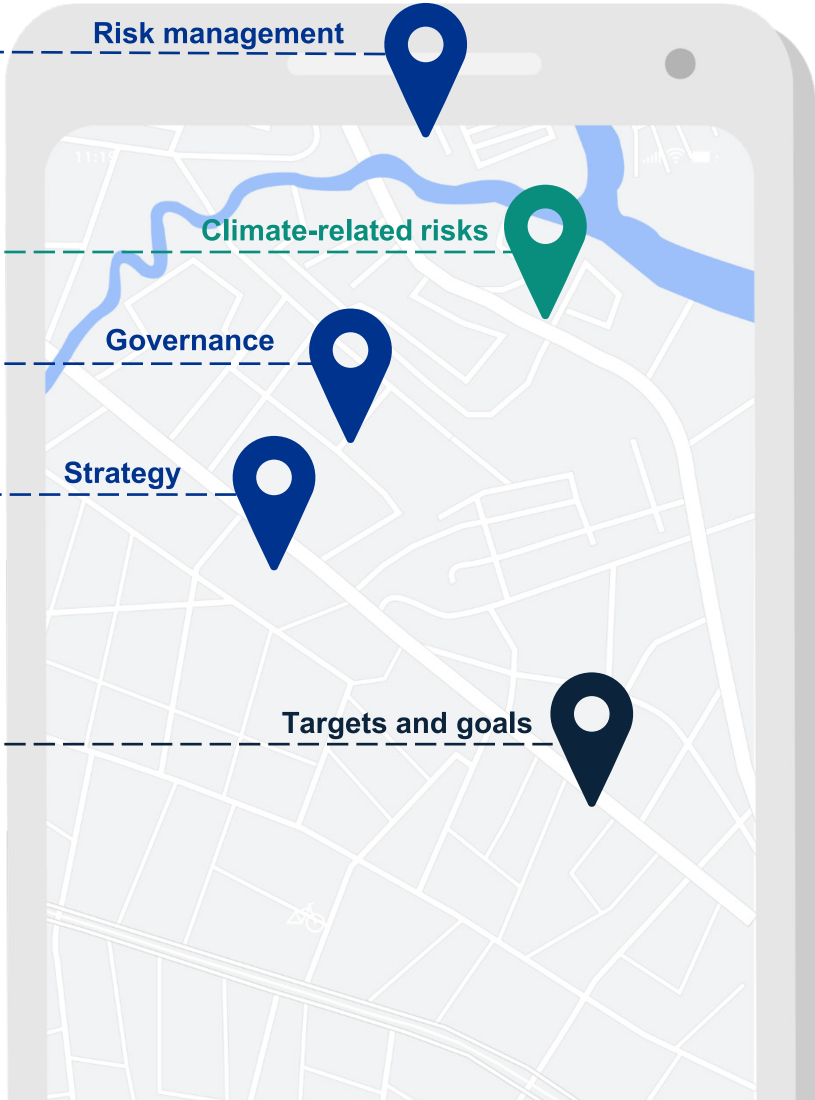
Scenario analysis: Relevant scenarios, parameters, assumptions, analytical choices, any expected material impacts

Internal carbon pricing: Price in units of reporting currency per metric ton CO_2e

Transition plan: Relevant metrics and targets used to identify and manage risks, plus progress

Targets and goals: Scope, unit of measurement, time horizon, progress to date

Offsets and RECs: Amount of carbon reduction or amount of renewable energy generated



If used and has a material effect

Safe harbor for forward-looking information, subject to conditions

Quantitative and qualitative disclosure of material expenditures incurred and impacts on financial estimates and assumptions deferred for one year (see Q8)

1) Collate all voluntary climate reporting and draft potential regulatory disclosure.

2) When identifying gaps, focus not only on the existence of information but also the quality of disclosure.

3) The SEC will continue to evaluate if information in public disclosures outside of the 10-K should have been filed.

4) Disclosure controls and procedures will need to expand to incorporate all new climate information (see Q7).

5) When evaluating if the information has a material effect, focus on qualitative factors.

6. How do the different disclosures connect?

Disclosure under Reg S-K:

— Climate-related targets or transition plans

— Climate-related targets or goals, and use of carbon offsets or RECs are a significant part of the plan to achieve such targets or goals

Disclosure in the financial statements:

— Capitalized costs and expenses related to the carbon offsets and RECs, and the relevant accounting policy

— Financial estimates or assumptions materially impacted by the disclosed targets or transition plans

Additional insight #1

Reg S-K also requires quantitative and qualitative disclosure of material expenditures incurred and impacts on financial estimates and assumptions (see Q5)

Additional insight #2

GHG emissions disclosures (see Q4) provide specific metrics to assess a registrant's exposure to transition risks

1) As progress is made against GHG reduction targets, consider how the organization achieved those reductions and the costs associated with the actions.

2) Leverage processes and controls to be implemented for the financial statement disclosures (see Q3).

3) Be wary of potentially contradictory evidence between disclosures in Reg S-K vs Reg S-X – e.g. a significant input in scenario analysis that is inconsistent or excluded from an asset impairment analysis.

7. What are the implications for controls?

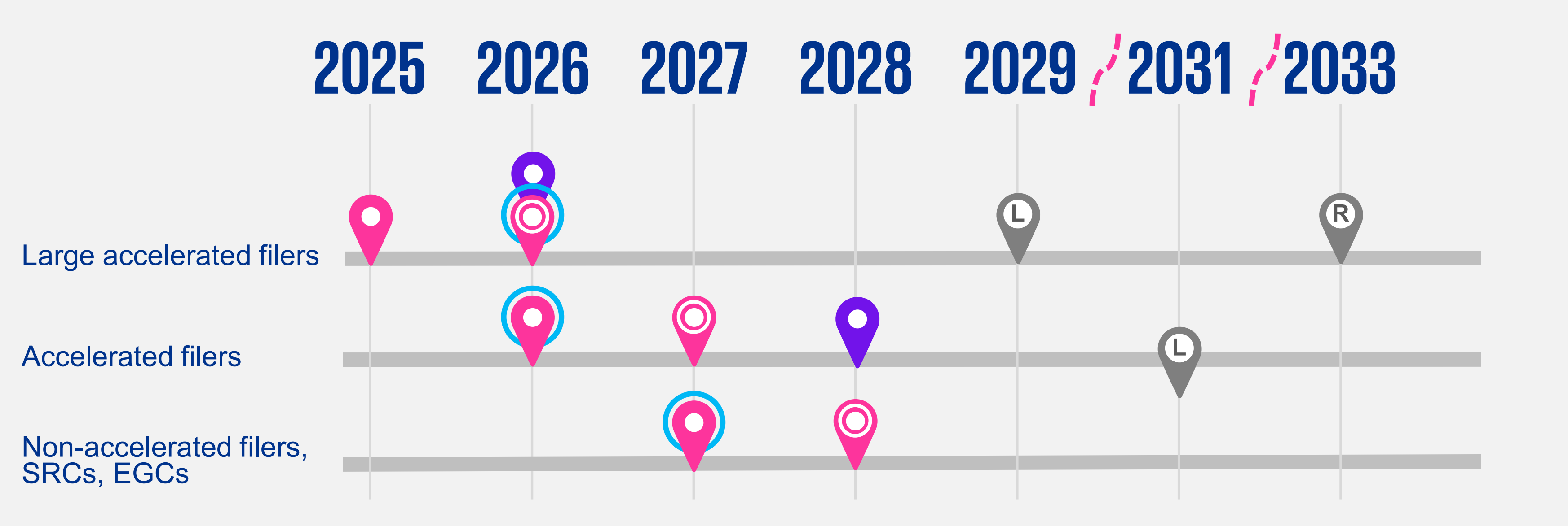
Controls and processes will need to be considered across the entire organization. As you develop new systems and processes or adjust existing ones, design and implement controls to withstand assurance of ICFR and GHG emissions.

These core elements of risk and controls programs apply to financial and nonfinancial data:

- Support for estimates, assumptions and disclosures
- Documented policies and procedures
- Evidence of secondary review and approval with appropriate thresholds
- Consistency across processes, methodologies, locations and countries
- Controls over third-party data
- Completeness and accuracy controls around key reports
- IT application and general controls
- Recalculation or validation procedures.

8. When must registrants comply?

ANNUAL DISCLOSURES FOR FISCAL YEARS BEGINNING IN CALENDAR YEAR:



- Financial statement disclosures (see Q3), and climate risk disclosures other than certain disclosures deferred for one year (see Q5)
- GHG emissions (see Q4)
- L Limited assurance of GHG emissions (see Q4)
- Disclosures that are deferred for one year (see Q5)
- Inline XBRL
- R Reasonable assurance of GHG emissions (see Q4)

1) Inventory possible climate-related disclosures provided in previous SEC filings even if they were written to comply with other regulations.

2) Using the phased transition as a guide, begin or update an analysis of what it would take operationally to comply with the final rules.

3) Coordinate with various stakeholders, including subsidiaries, who will provide the underlying data – and understand internal reporting timelines and obstacles to timely reporting.

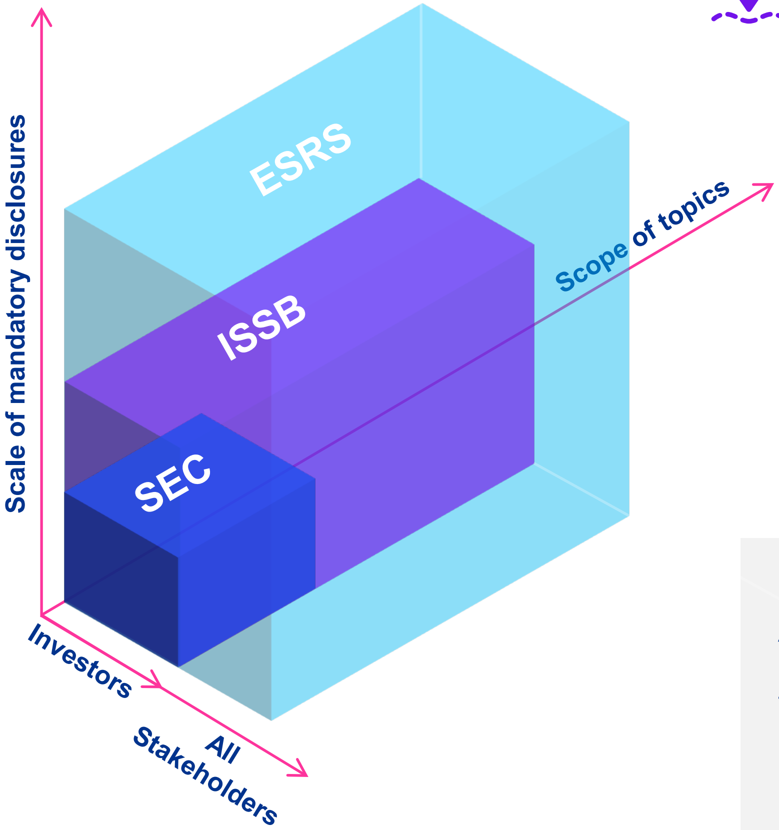
9. How do the rules compare to other frameworks?

Scope of topics

- **One component of sustainability:** The SEC focused on the disclosure of information about climate-related risks.
- **Vs broader range of sustainability topics:** Both ISSB Standards and ESRS span broader sustainability topics, although ESRS has a greater number of topic-specific standards.

Investors vs all stakeholders

- **Investor approach:** The SEC's remit is disclosures for the benefit of investors – similar to the approach under ISSB standards.
- **Vs multi-stakeholder approach:** ESRS are based on double materiality – considering both the investor and wider stakeholder lenses.



Scale of mandatory disclosures

- **Risk-based:** The SEC requires a number of targeted disclosures about risks, plus disclosures in the financial statements.
- **Vs broader disclosures:** ISSB Standards require more extensive disclosures about risks *and* opportunities, and ESRS additionally require disclosures about impacts. Neither require disclosures in the financial statements. All require calculation of financial impacts.

California

A majority of registrants in the scope of the SEC's climate rule are also in the scope of the California climate laws. The California disclosures are more onerous in some respects (e.g. Scope 3 GHG emissions) but allow flexibility in leveraging other sustainability reporting standards.

1) Taking these differences as foundational starting points, US companies currently preparing for compliance with ISSB Standards and/or ESRS are well positioned as they begin to analyze the SEC's climate rule.

2) For more insights, see our publication, Comparing sustainability reporting requirements.

3) To learn more about GHG reporting, see our Handbook, GHG emissions reporting.

KPMG

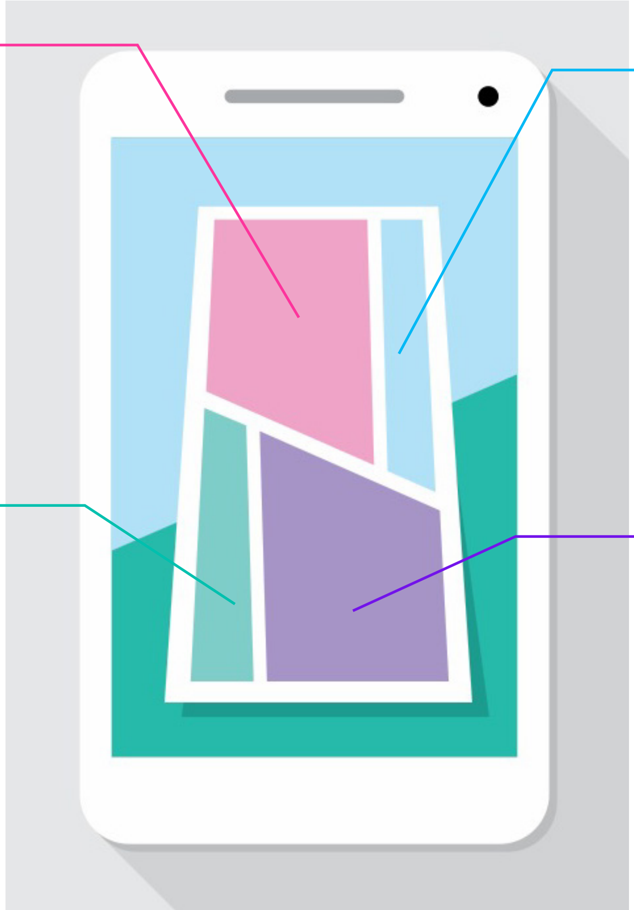
10. What do you need to do now?

General

- **Establish a plan, then educate** your organization on the requirements and response strategies you need to undertake – including the people, processes and technologies needed
- **Assess** how ready you are by evaluating how these rules compare with your existing voluntary climate reporting and global and local requirements

Financial statements

- **Determine** how to define and track expenditures and capitalized costs associated with severe weather events, other natural conditions and offsets / RECs
- **Evaluate** whether any estimates and assumptions are materially impacted by severe weather events, targets or transition plans



GHG disclosures

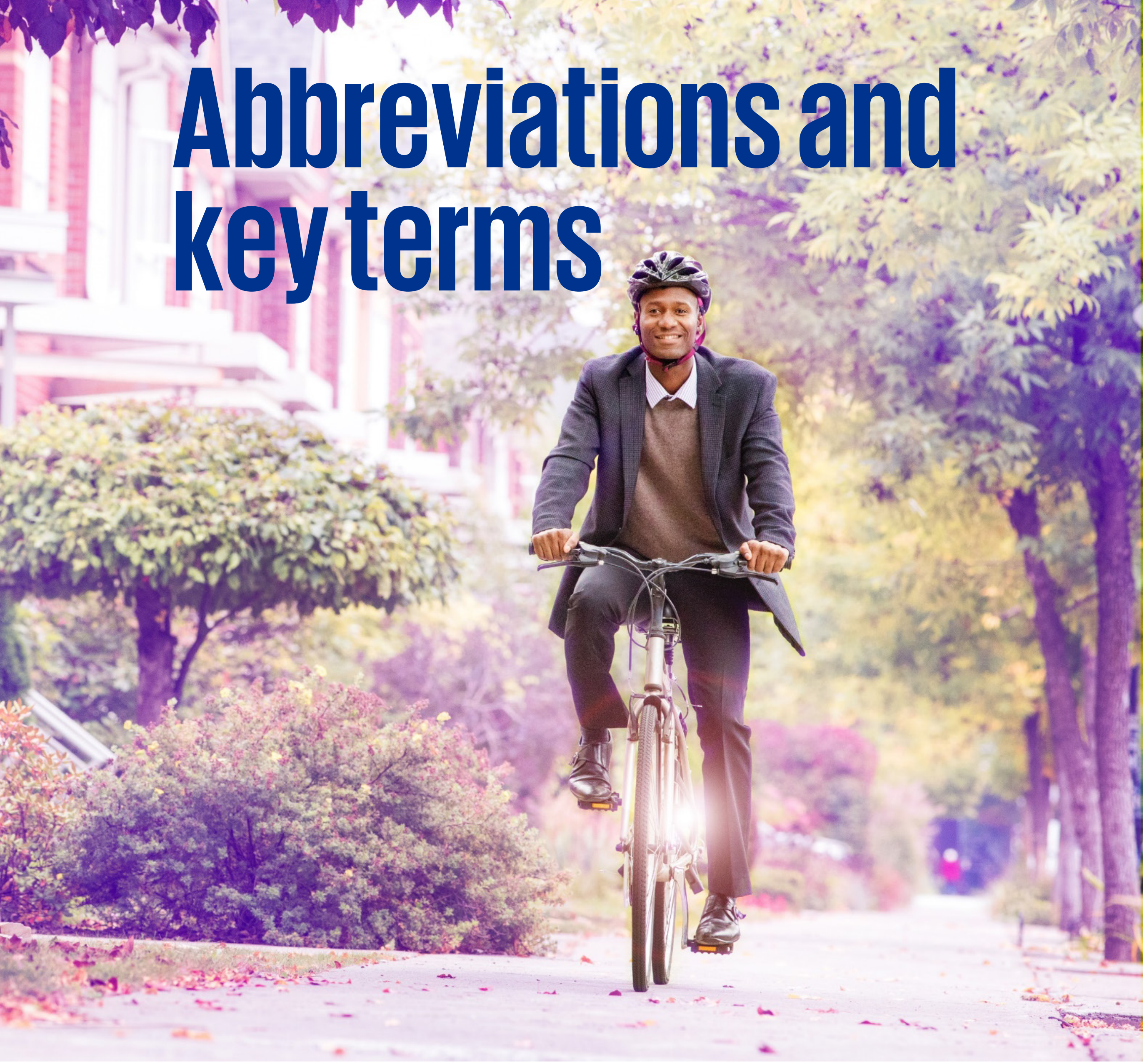
- **Develop or enhance** your GHG inventory and measure and disclose it in accordance with the requirements
- **Understand** current processes and controls around your GHG inventory and consider systemwide needs for automation of GHG emissions

Climate risk disclosures

- **Identify and tag** material expenditures that result from transition plans and targets or goals
- **Revisit** your enterprise risk assessment to identify climate-related risks that are considered material in the context of the rules

1) If you are currently preparing for compliance with other required sustainability frameworks (see Q9), evaluate how these new rules impact your ongoing implementation.
2) As you begin or continue along your journey, focus not only on complying but identifying opportunities to drive a competitive advantage.
3) Monitor the FASB's project on accounting for environmental credit programs.
4) We believe in the bigger picture – sustainability reporting is an opportunity to unlock value and not simply a compliance exercise.

Abbreviations and key terms



EGC
Emerging growth company

ESG
Environmental, Social, Governance

ESRS
European Sustainability Reporting Standards

FPIs
Foreign private issuers

GHG (greenhouse gas) emissions

Scope 1: Direct GHG emissions from operations that are owned or controlled by a registrant.

Scope 2: Indirect GHG emissions from the generation of purchased or acquired electricity, steam, heat or cooling that is consumed by operations owned or controlled by a registrant.

Scope 3: All indirect GHG emissions not otherwise included in a registrant's Scope 2 emissions, which occur in the upstream and downstream activities of a registrant's value chain.

ICFR
Internal control over financial reporting

ICSR
Internal control over sustainability reporting

IPO
Initial public offering

ISSB
International Sustainability Standards Board

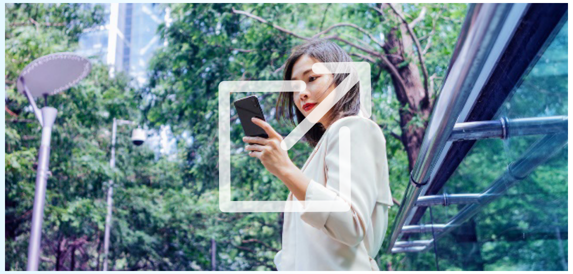
MJDS
Multijurisdictional Disclosure System

REC
Renewable energy certificate

SRC
Smaller reporting company

Resources

KPMG ESG helps your company create a more sustainable future while driving measurable growth today.



KPMG ESG Assurance provides insights that help your business in this new era of sustainability reporting.

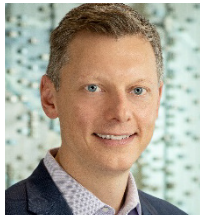
KPMG Financial Reporting View delivers ESG insights and guidance for financial reporting professionals.

KPMG insights on sustainability reporting under IFRS® Sustainability Disclosure Standards, including a comparison to ESRS and the SEC's climate rule.

Sign up for ESG alerts at visit.kpmg.us/KPMG-ESG

Keep in touch

Maura Hodge
Partner
KPMG US Audit ESG Leader
mhodge@kpmg.com



Sam Jeffery
Partner
KPMG US ESG Reporting Leader
samueljeffery@kpmg.com

Julie Santoro
Partner
KPMG US Dept. of Professional Practice
jsantoro@kpmg.com

With thanks to our additional contributors

Uju Akaegbobi	Marissa Gerdes	Louise Santacruz
Timothy Brown	Kalyan Karri	Alvamerry Schaefer
Anita Chan	Erin McCloskey	Angie Storm
Bryce Ehrhardt	Dyan Rohol	Catarina Vieira

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

Learn about us: **kpmg.com**